Year Ended December **31,2000 vs.**
Year Ended December **31,2001**

Revenues. Revenues for 2001 decreased 15.3% to $13.8 billion versus $16.3 billion for 2000. The decrease in total revenues is primarily attributable to consumers' substitution of wire line services with wireless and e-mail, and proactive revenue initiatives resulting in services being de-emphasized as we shift the MCI group's focus from revenue growth to cash generation.

Reported revenues by category for 2000 and 2001 reflect the following changes by category (dollars in millions):

	2000	2001	Percent Change
Consumer..	$ 7,778	$ 7,227	(7.1)
Wholesale	3,388	2,641	(22.0)
Alternative channels and small business	3,541	2,427	(31.5)
Dial-up Internet	1,628	1,536	(5.7)
Total..	$16,335	$13,831	(15.3)

Consumer revenues for 2001 decreased 7.1% over 2000. The majority of this decrease is attributed to decreases in calling card, dial around and dial-I revenues as a result of consumers' substitution of wire line services with wireless and e-mail. Our consumer local initiatives continued to perform well as consumer local revenues increased approximately 180% for 2001 versus 2000.

Wholesale revenues for 2001 decreased 22.0% over 2000. The wholesale market continued to be extremely price competitive and this, in addition to bankruptcies, a reduction in private line circuits related to customer internal network consolidation and the impact of the September 11th attacks, contributed to the year-over-year decrease. Wholesale revenues during 2001 were also impacted by proactive revenue initiatives, which were made to improve the quality of the wholesale revenue stream as we shift the MCI **group's** focus from revenue growth to cash generation.

Alternative channels and small business revenues for 2001 decreased 31.5% over 2000. Alternative channels and small business includes sales agents and affiliates, wholesale alternative channels, small business, prepaid calling card and wireless messaging revenues. These decreases are attributed to pricing pressures in the wholesale and small business markets which negatively affected revenue growth and gross margins in this area, and proactive initiatives to de-emphasize services with unacceptable gross margins as we shift the MCI group's focus from revenue growth to cash generation.

Dial-up Internet revenues for 2001 decreased 5.7% over 2000. **Our** dial access network has grown 12.7% to approximately 3.2 million modems as of December 31, 2001, compared with the prior year period. Additionally, Internet connect hours increased 9.3% to 7.1 billion hours for 2001 versus 2000. These network usage increases were more than offset by pricing pressure resulting from the impact of volume discounts, which lowered average revenue per hour by approximately 17% for 2001 versus 2000.

Line costs. Line costs as a percentage of revenues for 2001 increased to 51.2% as compared to 43.9% reported for 2000. The increase was primarily the result of continued competitive pricing in the dial-up Internet business as noted above, which experienced a 17% decrease in dial-up revenues **per** hour for 2001 versus 2000. Additionally, line costs as a percentage of revenues increased as a result of pricing pressure in the wholesale markets as well as the decrease in higher margin calling card and dial around revenues due to wireless substitution as noted above.

Selling, general and administrative. Selling, general and administrative expenses for 2001 were $5.3 billion or 38.7% of revenues as compared to $5.2 billion or 31.6% of revenues for the prior year period. Selling, general and administrative expenses for 2000 include a $345 million pre-tax charge associated with specific wholesale accounts that were deemed uncollectible due to bankruptcies, litigation and settlements of contractual disputes that occurred in the third quarter of 2000. Selling, general and administrative expenses for 2001 include pre-tax costs of $123 million related to the write-off of investments in certain publicly traded and privately held companies, $11 million as a result of the costs associated with the tracking stock capitalization and $48 million associated with domestic severance packages and other costs related to our February 2001 workforce reductions. Excluding these costs, selling, general and administrative expenses as a percentage of revenues were 37.4% for 2001 versus 29.5% for 2000.

The increase in selling, general and administrative expenses can be attributed to proactive initiatives to de-emphasize specific wholesale services revenues with unacceptable gross margins which began in the fourth quarter of 2000. These actions resulted in lower revenues, as discussed above, but had no immediate effect on selling, general and administrative expenses for both the wholesale and alternative channels. Workforce reductions in the first quarter of 2001 have helped to stabilize selling, general and administrative expenses since the second quarter of 2001.

Depreciation nnd amortization. Depreciation and amortization expense for 2001 increased to $938 million or 6.8% of revenues from $884 million or 5.4% of revenues for 2000. The increase primarily reflects additional depreciation associated with 2000 and 2001 capital expenditures. Beginning January 1, 2002, MCI group stopped amortizing intangible assets with indefinite useful lives, including goodwill in accordance with SFAS No. 142. Based on current levels of such assets, this will reduce MCI group's amortization expense by approximately $300 million annually.

Interest expense. Interest expense for 2001 was $504 million or 3.6% of revenues as compared to $512 million or 3.1% of revenues for 2000. Interest expense on borrowings incurred by WorldCom and allocated to the MCI group was based on the weighted-average interest rate, excluding capitalized interest, of WorldCom debt plus 1¼ percent. As of January 1, 1999, $6.0 billion of WorldCom's outstanding debt was notionally allocated to the MCI group. During 2001, the MCI group repaid $495 million of the notionally allocated debt and as of Deccmber 31, 2001 the MCI group's long-term debt balance was $5.5 billion.

Income tax benefit. The effective income tau rate was 41.0% of loss before taxes for 2001 versus 39.8% of income before taxes for 2000. See note 8 to the MCI group's combined financial statments for a reconciliation of the statutory federal rate for income taxes to the MCI group's effective income tax rate.

Cumulative effect of accounting change. During 2000, we adopted SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather than be recognized immediately. Costs directly related to these revenues may also be deferred and amortized over the customer contract life. This adoption resulted in a one-time expense of $10 million, net of income tax benefit of $7 million for the MCI group in the first quarter of 2000.

Net income (loss). For 2001, the MCI group reported a net loss of $23 million as compared to net income of $1.6 billion for 2000. Pro forma diluted loss per common share for 2001 was $0.20 compared to income per common share of $13.52 for 2000. Pro forma diluted income per share assumes the recapitalization occurred at the beginning of 2000 and that the WorldCom group stock and MCI group stock existed for all periods presented.

Year Ended December 31, 1999 vs.
Year Ended December 31,2000

Revenues. Revenues for 2000 increased 1.0% to $16.3 billion versus $16.2 billion for 1999. The increase in total revenues is attributable to internal growth of the MCI group.

Reported revenues by category for the year ended December 31, 1999 and 2000 reflect the following changes by category (dollars in millions):

	1999	2000	Percent Change
Consumer..	$ 7,590	$ 7,778	2.5
Wholesale	3,943	3,388	(14.1)
Alternative channels and small business	3,142	3,541	12.7
Dial-up Internet	1,497	1,628	8.8
Total revenues	$16,172	$16,335	1.0

Consumer revenues **for** 2000 increased 2.5% over 1999, as the **MCI** group's partner marketing programs helped to drive Dial-1 product gains. Consumer revenue growth was impacted by declines in transaction brands and calling card services, which were pressured by increasing wireless substitution, and 10-10-321, which the **MCI** group no longer actively markets.

Wholesale revenues for 2000 decreased 14.1% versus 1999 as a result of price pressure. Wholesale revenues for 2000 were **also** impacted by proactive fourth quarter 2000 revenue actions which had the effect of reducing wholesale revenues by approximately $90 million in the fourth quarter of 2000. These actions were made to improve the quality of the wholesale revenue stream as we shift the MCI group's focus from revenue growth to cash generation.

Alternative channels and small business revenues for 2000 increased 12.7% over 1999. **This** increase is primarily attributable to internal growth for wholesale alternative channel voice revenues. **We** expect that pricing pressures in **the** wholesale and small business markets will negatively affect revenue growth and gross margins in this area and this level of growth will decline in the foreseeable future as a result of these services being de-emphasized as we shift the **MCI** group's focus from revenue growth to cash generation.

Dial-up Internet revenue growth for 2000 was 8.8% over 1999. Our dial access network has grown 71% to over 2.8 million modems **as** of December 31, 2000, compared with 1999. Additionally, Internet connect hours increased 54.8% to 6.5 billion hours for 2000 versus the prior year. These network usage increases were offset by pricing pressure on dial-up Internet traffic **as** a result of contract repricings in the second quarter of 2000, which lowered average revenue per hour by 25% for 2000 versus 1999.

Line costs. Line costs as a percentage of revenues for 2000 increased to 43.9% as compared to 43.8% reported for the prior year period. The increase was primarily the result of contract repricings in the dial-up Internet business **as** noted above and continued competitive pricing on the dial-up Internet business which effectively held the average 'Cost per hour constant although average dial-up Internet revenues per hour decreased by 25%. Additionally, **access** charge reductions that occurred in January 2000 and July **2000** reduced total line costs by approximately $150 million for 2000. While access charge reductions were primarily passed through to customers, line costs **as** a percentage of revenues was positively affected hy one-half of a percentage point.

Selling, general** and **administrative. Selling, general and administrative expenses for 2000 were $5.2 billion or 31.6% of revenues **as** compared to $5.1 billion or 31.4% of revenues for the prior year period. Selling, general and administrative expenses **for** 2000 include a $345 million pre-tax charge associated with specific wholesale accounts that were deemed uncollectible due to bankruptcies, litigation and settlements of contractual disputes that occurred in the third quarter of 2000. Excluding this charge, selling, general and administrative expenses **as** a percentage of revenues were 29.5% for 2000. This decrease as a percentage of revenues primarily results from lower advertising and marketing costs incurred in the consumer business.

Depreciation and amortization. Depreciation and amortization expense for 2000 increased to $884 million or 5.4% of revenues from $757 million or 4.7% of revenues for 1999. These increases primarily reflect additional depreciation associated with capital expenditures.

Interest expense. Interest expense for 2000 was $512 million or 3.1% of revenues as compared to $506 million or 3.1% of revenues for 1999. Interest expense on borrowings incurred by WorldCom and allocated to the MCI group was based on the weighted-average interest rate, excluding capitalized interest, of WorldCom debt plus 1¼ percent. As of January 1, 1999, $6.0 billion of WorldCom's outstanding debt was notionally allocated to the MCI group.

Miscellaneous income and expense. For the year ended December 31, 2000, miscellaneous income was zero as compared to $5 million for 1999.

Provision for income taxes. The effective income tax rate for 2000 was 39.8% of income before taxes. The 2000 rate is greater than the expected federal statutory rate of 35% primarily due to the amortization of the non-deductible goodwill. Excluding non-deductible amortization of goodwill, the MCI group's effective income tax rate would have been 36.7%.

Cumulative effect of accounting change. During the fourth quarter of 2000, we implemented SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather than be recognized immediately. Costs directly related to these revenues may also be deferred and amortized over the customer contract life. As required by SAB 101, we retroactively adopted this accounting effective January 1, 2000, which resulted in a one-time expense of $10 million, net of income tax benefit of $7 million at the MCI group.

Net income. For the year ended December 31, 2000, the MCI group reported net income of $1.56 billion as compared to $1.65 billion for the year ended December 31, 1999.

Liquidity and Capital Resources

As of December 31, 2001, our total debt, net of cash and cash equivalents, was $28.8 billion. Additionally, at December 31, 2001, we had available liquidity of $9.4 billion under our credit facilities and commercial paper program and cash on hand.

As of January 1, 1999, the MCI group was notionally allocated $6.0 billion of WorldCom's debt and the remaining outstanding debt was notionally allocated to the WorldCom group. WorldCom management has a wide degree of discretion over the cash management policies of both the WorldCom group and the MCI group. Cash generated by either group can be transferred to the other group without prior approval of WorldCom's shareholders. Due to the discretion possessed by management over the cash management policies of both groups, including the timing and decision of whether to finance capital expenditures, it may be difficult to assess each group's liquidity and capital resource needs, and, in turn, the future prospects of each group based on past performance. For 2001, the MCI group generated sufficient cash to repay $495 million of its allocated notional debt and pay $71 million for dividends on MCI group stock.

On June 8, 2001, we replaced our existing $7 billion 364-Day Revolving Credit and Term Loan Agreement with two new credit facilities consisting of a $2.65 billion 364-Day Facility, and a $1.6 billion Multi-Year Facility. The 364-Day Facility and the Multi-Year Facility, together with our $3.75 billion Existing Facility, provide us with aggregate credit facilities of $8 billion. These credit facilities provide liquidity support for our commercial paper program and for other general corporate purposes.

The Existing Facility and the Multi-Year Facility mature on June 30, 2002 and June 8, 2006, respectively. The 364-Day Facility has a 364-day term, which may be extended for successive 364-day terms to the extent of the committed amounts from those lenders consenting thereto, with a requirement that lenders holding 51% of the committed amounts consent and so long as the final maturity date does not extend beyond June 8, 2006. Additionally, we may elect to convert the principal debt outstanding under the 364-Day Facility to a term loan maturing no later than one year after the conversion date, so long as the final maturity date does not extend beyond June 8, 2006. The Existing Facility is subject to annual commitment fees not to exceed 0.25% of any unborrowed portion of the facilities, and the current commitment fee is 0.11%. WorldCom does not intend to replace the Existing Facility when it matures on June 30, 2002. The 364-Day Facility and the Multi-Year Facility are subject to annual facility fees not to exceed 0.20% or 0.25%, respectively, of the average daily commitment under each such facility (whether used or unused). The current commitment fee on the 364-Day Facility is 0.07% and the current commitment fee on the Multi-Year Facility is 0.09%.

The credit facilities bear interest payable in varying periods, depending on the interest period, not to exceed six months, or with respect to any Eurodollar Rate borrowing, 12 months if available to all lenders, at rates selected by us under the terms of the credit facilities. including a Base Rate or Eurodollar Rate, plus the applicable margin. The applicable margin for the Eurodollar Rate borrowing generally varies from 0.35% to 0.75%, and is currently set at 0.35%, as to loans under the Existing Facility, from 0.29% to 0.80%, and is currently set at 0.33% as to loans under the 364-Day Facility and 0.27% to 0.75%, and is currently set at 0.31% as to loans under the Multi-Year Facility, in each case based upon our then current debt ratings.

The credit facilities are unsecured and require compliance with various covenants including a financial covenant based on the ratio of total debt to total book capitalization, which may not exceed 0.68 to 1.00, calculated on a consolidated basis. The credit facilities also require compliance with various operating covenants which, among other things, permit the following transactions so long as we are not in default thereunder:

- distributions to shareholders;
- the incurrence of additional indebtedness, except that newly secured debt or the total debt of the covered subsidiaries, cannot exceed 10% of the book value of the consolidated assets of WorldCom and the covered subsidiaries; and
- sales of assets in the ordinary course of business and additional sales if after such sales, the aggregate book value of all such assets sold during the term of the credit facilities does not exceed 20% of the book value of the consolidated assets of WorldCom and the covered subsidiaries.

As of the date of this filing, we were in compliance with these covenants.

On May 9, 2001, we completed the pricing of a public debt offering of approximately $11.9 billion principal amount of debt securities, based on currency exchange rates on May 8, 2001. The net proceeds of $11.7 billion have been or will be used for general corporate purposes, including the repayment of commercial paper and other debt repayments as outlined below. The public debt offering consisted of the following series of notes:

	Principal Amount	Maturity	Interest Payable	First Interest Date
6.50% Notes due 2004	$ 1.5 billion	May 15, 2004	Semiannually	November 15, 2001
7.50% Notes due 2011.	$ 4.0 billion	May 15, 2011	Semiannually	November 15, 2001
8.25% Notes due 2031	$ 4.6 billion	May 15, 2031	Semiannually	November 15, 2001
6.75% Notes due 2008.	€ 1.25 billion	May 15, 2008	Annually	May 15, 2002
7.25% Notes due 2008.	£ 500 million	May 15, 2008	Annually	May 15, 2002

All of the notes, except for the 6.50% Notes due 2004 are redeemable, as a whole or in part, at our option, at any time or from time to time, at respective redemption prices equal to the greater of 100% of the principal amount of the notes to be redeemed or:

- In the case of the **U.S.** dollar notes, the sum of the present values of the Remaining Scheduled Payments, as defined therein, discounted, on a semiannual basis, assuming a 360-day year consisting of twelve 30-day months, at the Treasury Rate, **as** defined therein, **plus:**
  - 30 basis points for the Notes due 2011, and
  - 35 basis points for the Notes due 2031;
- In the case of the euro notes, the sum of the present values of the Remaining Scheduled Payments, as defined therein, discounted, on an annual basis (based on the actual number of days elapsed divided **by** 365 or 366, as the case may be), at the Reference Euro Dealer Rate, as defined therein, **plus** 25 basis points; and
- In the case of the sterling notes, the price expressed as a percentage (rounded to three decimal places, with .0005 being rounded **up)** at which the Gross Redemption Yield, as defined therein, on the outstanding principal amount of the notes on the Reference Date, as defined therein, is equal to the Gross Redemption Yield (determined by reference to the middle-market price) at 3:00 p.m. (London time) on that date on the Benchmark Gilt, as defined therein, **plus** 25 basis points;

plus, in the case of the **U.S.** dollar notes, the euro notes and the sterling notes, accrued interest to the date of redemption which has not been paid.

In connection with the Intermedia merger, we assumed Intermedia's outstanding debt including $1.2 billion of senior discount notes with interest rates ranging from 11.25% to 12.5%, $0.9 billion **of** senior notes with interest rates ranging from 8.5% to 9.5%, credit facility borrowings of $258 million and other long-term debt including capital leases of $0.6 billion. We repaid the Intermcdia credit facility borrowings of $258 million and subsequently terminated Intermedia's credit facility during the third quarter of 2001. Additionally, on September 28, 2001, we redeemed all of Intermedia's 12.5% senior discount notes for $337 million. Cash balances were used to repay these amounts.

During the third and fourth quarters **of** 2001, $1.5 billion **of** 6.125% senior notes matured, $917 million **of** floating rate notes matured, we redeemed all of our outstanding 8.875% senior notes due 2006 for $694 million, we retired $1.1 **billion** of **our** outstanding debt through open market debt repurchases (including $546 million of outstanding debt assumed in the Intermedia merger) and we redeemed all of our outstanding Series ***G*** preferred stock at par for $200 million. Cash balances were used to repay these amounts.

Included in WorldCom long-term debt is a $700 million 6.125% senior note due 2012, which is a remarketable instrument. On April 15, 2002, the underwriter has an option to remarket the note and we have the option to accept the remarketing, exchange the note for new 5, 7 or 10-year notes at prevailing interest rates or redeem the note for cash. Since the note matures in 2012, it is not included in our 2002 scheduled debt maturities of $172 million.

Additionally, in February 2002, we liquidated our remaining investment in **News** Corporation. We received cash proceeds of $870 million, net of $60 million for sales discounts and banking fees. The investment's book value as of December 31, 2001 was approximately $930 million. Therefore, a **loss** of $60 million will be recognized in miscellaneous income (expense) in the first quarter of 2002 related to this transaction.

Our senior debt is currently rated as follows:

Rating Agency	Rating	Outlook
Moody's Investors Service	A3	Under review
Standard & Poor's	BBB+	Negative
Fitch Ratings	BBB+	Stable

Any downgrade in rating will not trigger any events on our outstanding bond debt, although the cost of future bond offerings may increase. Our credit facilities contain ratings triggers affecting interest rates and our annual commitment fee, which are outlined above and are not liquidity triggers. Additionally, if WorldCom merges or consolidates with another corporation, the surviving corporation, after giving effect to the merger or consolidation, among other things, must have a then effective debt rating equal to or higher than Baa3 by Moody's and BBB– by Standard & Poor's. Further, our $2 billion receivables purchase program contains rating triggers which reduce the availability under the program, and if we are rated less than Baa3 by Moody's and less than BBB- by Standard & Poor's, or if we are not rated by either agency, then the receivables purchase program is terminated. Our management frequently communicates with the rating agencies and currently believes that a downgrade below Baa3 or BBB– is not likely.

Operating activities

For the years ended December 31, 1999, 2000 and 2001, our cash flows from operations were as follows (dollars in millions):

	1999	2000	2001
WorldCom group	$ 7,352	$ 5,330	$6,605
MCI group	3,653	2,336	1,389
Net cash provided by operating activities	$11,005	$ 7,666	$7,994

The 2001 increase reflects decreases in accounts receivable and other working capital requirements, offset by lower operating results in both the WorldCom group and the MCI group. The 2000 decrease reflects increases in working capital requirements and deferred tax obligations in both the WorldCom group and the MCI group, offset by improved operating results in the WorldCom group.

Investing activities

For the years ended December 31, 1999, 2000 and 2001, our net cash used in investing activities was as follows (dollars in millions):

	1999	2000	2001
WorldCom group	$(8,045)	$(13,612)	$ (8,818)
MCI group	(1,510)	(773)	(872)
Net cash used in investing activities	$(9,555)	$(14,385)	$ (9,690)

The WorldCom group's primary capital expenditures totaled $7.9 billion in 1999, $11.0 billion in 2000 and $7.6 billion in 2001. Primary capital expenditures include purchases of transmission, communications and other equipment. The MCI group's capital expenditures totaled $787 million in 1999, $500 million in 2000 and $267 million in 2001. The MCI group's capital expenditures include purchases of switching equipment, dial modems and messaging and other equipment.

Investing activities include intangible asset increases at the WorldCom group of $389 million in 1999, $771 million in 2000 and $367 million in 2001, and at the MCI group of $354 million in 1999, $167 million in 2000 and $327 million in 2001. Intangible asset additions primarily represent costs incurred to develop softwarc for internal use.

Additionally, investing activities include acquisitions and related costs at the WorldCom group of $786 million in 1999, $14 million in 2000 and $206 million in 2001 and $292 million at the MCI group in 1999.

Financing activities

For the years ended December 31, 1999, 2000 and 2001, cash provided by (used in) financing activities was as follows (dollars in millions):

	1999	2000	2001
WorldCom group	$ 17	$ 8,215	$ 3,080
MCI group	(2,097)	(1,592)	(551)
Net cash provided by (used in) financing activities	$(2,080)	$ 6,623	$ 2,529

Financing activities include net repayments on debt of $2.9 billion in 1999 and net proceeds on borrowings on debt of $6.4 billion in 2000 and $3.0 billion in 2001. Financing activities for the MCI group reflect the repayments of intergroup advances, repayment of notionally allocated debt from WorldCom and dividends paid.

Also included in financing activities are proceeds from WorldCom's common stock issuances of $886 million in 1999, $585 million in 2000 and $124 million in 2001 as a result of WorldCom common stock option and warrant exercises.

Distributions on company obligated mandatorily redeemable and other preferred securities and dividends paid on other equity securities were $72 million in 1999, $65 million in 2000 and $154 million in 2001. The 2001 increase represents dividends associated with our Series D, E, F and G preferred stock which was issued in connection with the Intermedia merger, and dividends paid on MCI group stock.

In January 2000, each share of our Series C Preferred Stock was redeemed by us for $50.75 in cash, or approximately $190 million in the aggregate. Additionally, on August 20,2001 the holder of our Series G preferred stock exercised its right to require us to redeem all of the outstanding Series G preferred stock at par for $200 million.

In October 2001, we exercised our option to redeem all of our outstanding Series B Preferred Stock. Prior to the redemption date, substantially all of the holders of our Series B Preferred Stock elected to convert the preferred stock into 0.1460868 shares of WorldCom group stock and 0.005843472 shares of MCI group stock for each share of Series B Preferred Stock held.

During the second quarter of 2001, we declared the initial quarterly dividend for the MCI group stock. A cash dividend of $0.60 per share of MCI group stock, or approximately $70 million in the aggregate, was paid on October 15, 2001 to shareholders of record as of the close of business on September 28, 2001. Dividends of $0.60 per share of MCI group stock were also declared during the third and fourth quarters of 2001 which have been or will be paid in 2002.

The development of our businesses and the installation and expansion of our domestic and international networks will continue to require significant capital expenditures. For 2002, the WorldCom group capital expenditures are expected to be between $5.0 and $5.5 billion and the MCI group capital expenditures and intangible (softwarc development) spending are expected to be approximately $500 million.

We believe that cash flow from operations and available liquidity, including our credit facilities and commercial paper program and available cash will be sufficient to meet our capital needs, debt service and dividend requirements for the next twelve months. However, economic downturns and other adverse developments, including factors beyond our control, could impair our ability to service our indebtedness.

Critical accounting policies

Our significant accounting policies are described in Note 1 to the consolidated and combined financial statements included in Item 8 of this Form 10-K. We believe some of our most critical accounting policies include:

- estimating valuation allowances and accrued liabilities associated with revenue reserves and provisions for uncollectible accounts and pending litigation and regulatory matters;
- accounting for income taxes;
- goodwill and intangibles;
- valuation of long-lived and intangible assets, and goodwill;
- estimating depreciation and amortization associated with long-lived assets; and
- allocation policies between the Worldcom group and the MCI group

Estimating valuation allowances and accrued liabilities. The preparation of our consolidated financial statements requires us to make estimates and assumptions that affect the reported amount of assets and liabilities as well as the reported amounts of revenues and expenses for the periods presented. Specifically, our management must make estimates of future customer credits through the analysis of historical trends and known events. Significant management judgments and estimates must be made and used in connection with establishing the revenue reserves associated with discounts earned on special customer agreements, billing reserves for pricing changes and customer disputes. Material differences may result in the amount and timing of our revenue adjustments if management projections differ from actual results. Similarly, our management must make estimates regarding the collectibility of our accounts receivable. Management specifically analyzes accounts receivable including historical bad debts, customer concentrations, customer credit-worthiness and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. As of December 31, 2001, our accounts receivable balance was $5.3 billion, net of allowance for doubtful accounts of $1.1 billion.

We have recorded accruals for loss contingencies in our consolidated financial statements associated with legal and regulatory proceedings that are incidental to our business. Such accruals are based on our management's estimate of the projected liability and range of loss in accordance with applicable accounting guidance. Because of the uncertainties related to both the amount and range of loss on the remaining pending matters, management is unable to make a reasonable estimate of the ultimate liability related to an unfavorable outcome. As additional information becomes available, we will assess the potential liability related to our pending matters and revise our estimates. The results of these various legal and regulatory matters are uncertain and could have a material adverse affect on our consolidated results of operations or financial position.

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Accounting for income tares. As part of the process of preparing our consolidated financial statements we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves our estimating actual current tax exposure for WorldCom together with assessing temporary differences resulting from differing treatment of items, such as property, plant and equipment depreciation, for tax and accounting purposes. Actual income taxes could vary from these estimates due to future changes in income tax law or results from final tax exam reviews.

Goodwill and intangibles. Purchase accounting requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair market value of the assets and liabilities purchased. In our recording of the lntermedia merger, we allocated the purchase price among certain identifiable intangible assets and goodwill based on third party appraisals.

Valuation of long-lived assets, goodwill and intangibles. We assess the impairment of identifiable intangibles, long-lived assets and goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the use of our assets or the strategy for our overall business;
- significant negative industry or economic trends;
- significant dcclinc in our stock price for a sustained period; and
- our market capitalization relative to net book value.

We determine any impairment by comparing the undiscounted future cash flows estimated to bc generated by those assets to their respective carrying amounts. In the event an impairment exists, a loss is recognized based on the amount by which the carrying value exceeds the fair value of the asset or group of assets. If quoted market prices for an asset are not available, fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involvcd. Losses on property and equipment to be disposed of are determined in a similar manner, except that fair market values are reduced for the cost to dispose.

As discussed below, SFAS No. 142, became effective on January 1, 2002 and as a result, we stopped amortizing approximately $45.0 billion of net goodwill and $1.0 billion of net tradenames. Based on our current levels of such assets, this will reduce amortization by approximately $1.3 billion annually. In lieu of amortization, we are required to perform an initial impairment review of our goodwill and tradenames in 2002 and an annual impairment review thereafter. We expect to complete our initial impairment review no later than the second quarter of 2002.

We currently estimate that we will record an impairment charge upon completion of the initial impairment review of approximately $15 to $20 billion, with approximately $1 billion at the MCI group.

Depreciation and amortization of long-lived assets. We assign useful lives for long-lived assets based on periodic studies of actual asset lives and our intended use for those assets. Any change in these asset lives would be reported in our statement of operations as soon as any change in estimate is determined. There have been no material changes in asset lives during the three years ended December 31,2001.

Allocation policies between the WorldCom group and the MCI group. The financial information for the WorldCom group and the MCI group reflect the performance of the businesses attributed to each group and includes the attribution and allocation of our assets, liabilities, revenues and expenses between the WorldCom group and the MCI group in accordance with our tracking stock policy. Our management believes that the attribution and allocation methods used are equitable and provide a reasonable estimate of the costs attributable to each group. However, it is not practical to determine whether the allocated amounts represent amounts that would have been incurred on a stand-alone basis. Our board of directors or any special committee appointed by our board of directors may, without shareholder approval, change the policies set forth in our tracking stock policy statement and may adopt additional policies or make exceptions with respect to the application of the policies described in our policy statement in connection with particular facts and circumstances, all as they may determine to be in the best interests of WorldCom. Our board is subject to fiduciary duties to all of WorldCom's shareholders as one group, not to the holders of any series of stock separately. These policies are discussed in this management's discussion and analysis of financial condition and results of operations as well as in note 1 of the notes to combined financial statements of the WorldCom group and the MCI group.

Related party transactions

We have entered into certain loan and guaranty arrangements involving Bernard J. Ebbers, WorldCom's President and Chief Executive Officer, principally relating to certain obligations to financial institutions secured by Mr. Ebbers' stock in WorldCom. Following recent declines in the closing price of the WorldCom group stock, the outstanding debt covered by the WorldCom guaranty in favor of Bank of America, N.A., or Bank of America, has been repaid and we have deposited with Bank of America approximately $35 million to collateralize a letter of credit used to support financing for which Mr. Ebbers is obligated. The underlying letter of credit is scheduled to expire on February 15, 2003, subject to renewal, extension or substitution.

WorldCom made aggregate payments of approximately $198.7 million to Bank of America pursuant to the guaranty, in addition to the deposit collateralizing the letter of credit. That amount, together with any amounts paid or costs incurred by us in connection with the letter of credit, plus accrued interest at a floating rate equal to that under one of our credit facilities, is payable by Mr. Ebbers to us on demand. The amount of such interest accrued through February 28,2002, is approximately $875.000 and the interest rate as of that date was 2.15% per annum.

In addition to the guaranty arrangements, we have also agreed to loan up to $165 million in principal amount to Mr. Ebbers. These loans are payable on demand and bear interest at floating rates equal to that under certain of our credit facilities. As of February 28, 2002, the aggregate principal amount of indebtedness owed by Mr. Ebbers to us under these loans was approximately $144.3 million. Accrued interest on these loans is approximately $5.5 million through February 28, 2002, at interest rates ranging from 2.14% to 2.16% per annum as of that date.

We have been advised that Mr. Ebbers has used, or plans to use, the proceeds of the loans from WorldCom principally to repay certain indebtedness under loans secured by shares of our stock owned by him and that the proceeds of such secured loans were used for private business purposes. The loans and guaranty by WorldCom were made following a determination that they were in the best interests of WorldCom and our shareholders in order to avoid additional forced sales of Mr. Ebbers' stock in WorldCom. The determination was made by our Compensation and Stock Option Committee as a result of the pressure on our stock price, margin calls faced by Mr. Ebbers and other considerations. Such actions were ratified and approved by our board of directors.

In connection with the transactions described above, and subject to certain limitations, and effective upon termination of restrictions under existing lending agreements, Mr. Ebbers pledged to WorldCom the shares of our stock owned by him with respect to his obligations under the loans and guaranty from WorldCom. The pledge of certain of those shares is subordinated to the prior rights of other lenders and is not currently perfected. Mr. Ebbers also agreed to indemnify WorldCom for any amounts expended or losses, damages, costs, claims or expenses incurred under the guaranty or the loans from WorldCom and has provided information demonstrating that his assets are sufficient to cover his outstanding obligations to us.

Contractual obligations and commitments

As of December 31, 2001, we had various contractual ohligations and commitments which are more fully disclosed in our notes to consolidated financial statements. Components of these obligations and commitments include:

- our long-term debt, which includes capital leases. The detail of our long-term debt maturities is outlined below under "Quantitative and qualitative disclosures about market risk";
- our operating leases for office facilities and equipment under non-cancelable operating leases having initial or remaining terms of more than one year and our obligations under rights-of-way and franchise agreements with various entities for use of their rights-of-way for the installation of our telecommunications systems. Total multi-year obligations under operating leases and rights-of-way are $3.9 billion and $443 million, respcctivcly, as of December 31, 2001;
- our outsourcing agreement with EDS pursuant to which we outsource portions of our information technology, or **IT,** operations to EDS. EDS has assumed responsibility for our IT system operations at more than a dozen of our processing centers worldwide. As of December 31, 2001, the contractual obligation associated with this multi-year contract was $2.4 billion in the aggregate;
- our obligations under contractual commitments with traditional local phone companies who provide ports to **us** in co-located facilities, which we use **for** dial-up Internet access. **As** of December 31, 2001, the contractual commitment associated with these contracts was $1.9 billion in the aggregate. During 2001, we were successful in the renegotiation of many of these contracts, at no cost, and as a result, the multi-year contractual commitment has been lowered by more than $1.1 billion versus the comparable obligation in 2000. We will recognize the benefits associated with these savings over the next three to five years; and
- our obligations associated with the purchase of special access circuits from traditional local phone companies under optional payment plans which are term and volume discounts off traditional local phone company standard pricing. At December 31, 2001, the remaining obligations associated with the optional payment discount plans are $1.8 billion.

For a detailed description of our long-term debt and further disclosure regarding leases and other commitments, please see note 4 and note **8** to our consolidated financial statements, which are incorporated herein hy reference.

Recently issued accounting standards

In June 2001, the FASB issued **SFAS** No. 141 "Business Combinations" and **SFAS** No. 142 "Goodwill and Other Intangible Assets." **SFAS** No. 141 requires business combinations initiated after June 30, 2001, which includes the Intermedia merger, to be accounted for using the purchase method of accounting and broadens the criteria for recording intangible assets separate from goodwill. Recorded goodwill and intangibles will he evaluated against this new criteria and may result in certain intangibles being subsumed into goodwill, or alternatively, amounts initially recorded as goodwill may be separately identified and recognized apart from goodwill. Under the new rules, goodwill and intangible assets deemed to have indefinite lives will no longer be amortized but will be subject to annual impairment tests. The statement includes provisions for the identification of reporting units for purposes of assessing potential future impairments of goodwill. Upon adoption, we stopped amortizing intangible assets with indefinite useful lives, including goodwill and tradenames. Based on current levels of such assets, **this** will reduce amortization expense by approximately $1.3 billion annually ($1.0 billion **at** WorldCom group and $0.3 billion at MCI group). Additionally, we are conducting impairment reviews of all intangibles assets with indefinite useful lives and we expect to complete this assessment no later than the second quarter of 2002, in accordance with the provisions of **SFAS** No. 142. Based on our preliminary analyses, we estimate that as a rcsult of the adoption of SFAS No. 142 we will reduce goodwill by $15 to $20 billion, with approximately $1 billion of the reduction at the MCI group.

In June 2001, the FASB issued SFAS No. 143 “Asset Retirement Obligations,” which establishes new accounting and reporting standards for legal obligations associated with retiring assets. The fair value of a liability for an asset retirement obligation must be recorded in the period in which it is incurred, with the cost capitalized as part of the related long-lived assets and depreciated over the asset’s useful life. Changes in the liability resulting from the passage of time will be recognized as operating expenses. SFAS No. 143 must be adopted by 2003. We have not yet quantified the impact of adopting SFAS No. 143 on our consolidated results of operations or financial position.

In August 2001, the FASB issued SFAS No. 144 “Accounting for the Impairment or Disposal of Long Lived Assets,” which supersedes both SFAS No. 121 ‘Accounting for the Impairment of Long-Lived Assets for Long-Lived Assets to be Disposed Of,” and the accounting and reporting provisions for the disposal of a segment of a business contained in APB Opinion No. 30, “Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions.” SFAS No. 144 establishes a single accounting model for long-lived assets to be disposed of by sale and broadens the presentation of discontinued operations. The provisions of SFAS No. 144 are effective beginning in 2002 and are not expected to have a material impact on our consolidated results of operations or financial position.

Euro conversion

On January 1, 2002, the national currencies of 12 out of the 15 member countries of the European Union werc replaced by the euro, a new common currency and legal tender. We have completed our work to address the many issues involvcd with thc introduction of the euro, including the conversion of information technology systems, recalculating currency risk, recalibrating other financial instruments, and implementing strategies concerning continuity of contracts. Our processes for preparing taxation and accounting records have been refined and we do not expect any additional significant costs to bc incurred as a result of any future changes or refinements we may consider necessary. We belicvc that our business might be affected in the future by the impact of increased price transparency, however, we expect to be able to maintain our margins across our international operations as a result of any pricing changes that we decide to make purely as a result of the introduction of the euro.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Currently, we do not use derivative financial instruments to manage our interest rate risk. We have minimal cash flow exposure due to general interest rate changes for our fixed rate, long-term debt obligations. We do not believe a hypothetical 10% adverse rate change in our variable rate debt obligations would be material to our results of operations. The tables below provide information about our risk exposure associated with changing interest rates on long-term debt obligations that impact the fair value of these obligations as of December 31, 2000 and 2001.

	Long-term Debt (in millions of dollars) as of December 31,2000					
Expected Maturity	**Fixed Rate**	**Average Interest Rate (%)**	**Variable Rate**	**Average Interest Rate (%)**	**Foreign Currency Denominated**	**Average Interest Rate (%)**
2001	$ 1,609	6.23	$5,129	7.06	$ 462	9.40
2002	74	7.75	60	7.30	333	9.29
2003	1,626	7.27	—	—	178	9.28
2004..	1,049	7.52	—	—	172	9.03
2005..	2,268	6.41	—	—	119	8.83
Thereafter..	11,481	7.49	—	—	336	9.47
Total..	$18,107		$5,189		$1,600	
Fair Value, December 31, 2000	$17,837		$5,188		$1,551	

	Long-tern Debt (in millions of dollars) as of December 31,2001					
Expected Maturity	**Fixed Rate**	**Average Interest Rate (%)**	**Variable Rate**	**Average Interest Rate (%)**	**Foreign Currency Denominated**	**Average Interest Rate (%)**
2002..	$ 88	8.68	$ 60	4.66	$ 24	8.94
2003	1,657	7.31	—	—	92	8.94
2004	2,565	6.94	—	—	57	8.92
2005	2,302	6.44	—	—	47	8.92
2006	2,613	7.64	—	—	30	8.92
Thereafter	18,548	7.71	—	—	2,127	7.21
Total.,	$27,773		$ 60		$2,377	
Fair Value, December 31, 2001	$28,481		$ 60		$2,441	

We are exposed to foreign exchange rate risk primarily due to other international operation's holding of approximately $512 million in U.S. dollar denominated debt, and our holding of approximately $1.9 billion of indebtedness indexed in other foreign currencies including the Euro and Pound Sterling as of December 31, 2001. Our potential immediate loss that would result from a hypothetical 10% change in foreign currency exchange rates based on this position would be approximately $209 million. In addition, if that change werc to be sustained, our cost of financing would increase in proportion to the change.

We are also subject to risk from changes in foreign exchange rates for our international operations which use a foreign currency as their functional currency and are translated into U.S. dollars.

Wc believc our market risk exposure with regard to our marketable equity securities is limited to changes in quoted market prices for the securities. Based upon the composition of our marketable equity securities at December 31, 2001, we do not believe a hypothetical 10% adverse change in quoted market prices would be material to our results of operations or financial position.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Consolidated Financial Statements and notes thereto are included elsewhere in this Annual Report on Form 10-K **as** follows:

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

PART 111

The information required by this Part III will be provided in our definitive proxy statement for our 2002 annual meeting of the shareholders (involving the election of directors), which definitive proxy statement will be filed pursuant to Regulation **14A** not later than 120 days following our fiscal ycar ended December 31, 2001, and **is** incorporated herein by this reference to the following extent:

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information under the captions "ELECTION OF DIRECTORS — Information about Nominees and Executive Officers" and "EXECUTIVE COMPENSATION—Section 16(a) Beneficial Ownership Reporting Compliance."

ITEM 11. EXECUTIVE COMPENSATION

The information under the captions "INFORMATION CONCERNING BOARD OF DIRECTORS — Compensation of Directors" and "EXECUTIVE COMPENSATION."

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information under the captions "PRINCIPAL HOLDERS OF VOTING SECURITIES" and "SECURITY OWNERSHIP OF MANAGEMENT."

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information under the caption "EXECUTIVE COMPENSATION — Certain Relationships and Related Transactions" and "INFORMATION CONCERNING BOARD OF DIRECTORS— Compensation of Directors."

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) 1 and 2

Financial statements and financial statement schedule

See Index to Consolidated Financial Statements and Financial Statement Schedule on page F-1. All other schedules for which provision is made in the applicable accounting regulations of the SEC are not required under the related instructions or are inapplicable and, therefore, have been omitted.

(a) 3

Exhibits required by Item 601 of Regulation **S-K**

See Exhibit Index for the exhibits filed as part of or incorporated by reference into this Annual Report on Form 10-K. There are omitted from the exhibits filed with or incorporated by reference into this Annual Report on Form **10-K** certain promissory notes and other instruments and agreements with respect to long-term debt of WorldCom, none of which authorizes securities in a total amount that exceeds 10% of the total assets of WorldCom on a consolidated basis. Pursuant to Item 601(b)(4)(iii) of Regulation **S-K,** we hereby agree to furnish to the SEC copies of any such omitted promissory notes or other instruments or agreements as the SEC requests.

(b) Reports on Form **8-K**

None

SIGNATURES

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WorldCom, Inc

By: /s/ SCOTT D. SULLIVAN

Scott D. Sullivan
Chief Financial Officer

Date: March 13, 2002

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Name	Title	Date
/s/ JAMES C. ALLEN James C. Allen	Director	March 13, 2002
/s/ JUDITH AREEN Judith Areen	Director	March 13, 2002
/s/ CARL J. AYCOCK Carl J. Aycock	Director	March 13, 2002
/s/ MAX E. BOBBITT Max E. Bobbitt	Director	March 13, 2002
/s/ BERNARD J. EBBERS Bernard J. Ebbers	Director, President and Chief Executive Officer (Principal Executive Officer)	March 13, 2002
/s/ FRANCESCO GALESI Francesco Galesi	Director	March 13, 2002
/s/ STILES A. KELLETT, JR. Stiles A. Kellett, Jr.	Director	March 13, 2002

Name	Title	Date
/s/ GORDON S. MACKLIN Gordon S. Macklin	Director	March 13, 2002
/s/ BERT C. ROBERTS, JR. Bert C. Roberts, Jr.	Chairman of the Board	March 13, 2002
/s/ JOHN W. SIDGMORE John W. Sidgmore	Director	March 13, 2002
/s/ SCOTT D. SULLIVAN Scott D. Sullivan	Director and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 13, 2002

INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders of WorldCom, Inc.:

We have audited the accompanying consolidated balance sheets of WorldCom, Inc. (a Georgia corporation) and subsidiaries as of December 31, 2000 and 2001, and the related consolidated statements of operations, shareholders' investment and cash flows for each of the years in the three-year period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of WorldCom, Inc. and subsidiaries as of December 31, 2000 and 2001, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

As discussed in Note 1 to the consolidated financial statements, effective January 1, 2000, the Company changed its method of accounting for certain activations and installation fee revenues and expenses.

ARTHUR ANDERSEN LLP

Jackson, Mississippi
March 7, 2002

WORLDCOM, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In Millions, Except Share Data)

	December 31, 2000	December 31, 2001
ASSETS		
Current assets:		
Cash and cash equivalents	$ 761	$ 1,416
Accounts receivable, net of allowance for bad debts of $1,532 in 2000 and $1,086 in 2001	6,815	5,308
Deferred tax asset	172	251
Other current assets	2,007	2,230
Total current assets	9,755	9,205
Property and equipment:		
Transmission equipment	20,288	23,814
Communications equipment	8,100	7,878
Furniture, fixtures and other	9,342	11,263
Construction in progress	6,897	5,706
	44,627	48,661
Accumulated depreciation	(7,204)	(9,852)
	37,423	38,809
Goodwill and other intangible assets	46,594	50,537
Other assets	5,131	5,363
	$ 98,903	$ 103.914
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
Current liabilities:		
Short-term debt and current maturities of long-term debt	$ 7,200	$ 172
Accrued interest	446	618
Accounts payable and accrued line costs	6,022	4,844
Other current liabilities	4,005	3,576
Total current liabilities	17,673	9,210
Long-term liabilities, less current portion:		
Long-term debt	17,696	30,038
Deferred tax liability	3,611	4,066
Other liabilities	1,124	576
Total long-term liabilities	22,431	34,680
Commitments and contingencies		
Minority interests	2,592	101
Company obligated mandatorily redeemable and other preferred securities	798	1,993
Shareholders' investment:		
Series B preferred stock, par value $.01 per share; authorized, issued and outstanding: 10,693,437 shares in 2000 and none in 2001 (liquidation preference of $1.00 per share plus unpaid dividends)	—	—
Preferred stock, par value $.01 per share; authorized: 31,155,008 shares in 2000 and 30,967,637 shares in 2001; none issued	—	—
Common stock		
WorldCom, Inc. common stock, par value $.01 per share; authorized: 5,000,000,000 shares in 2000 and none in 2001; issued and outstanding: 2,887,960,378 shares in 2000 and none in 2001	29	
WorldCom group common stock, par value $.01 per share; authorized: none in 2000 and 4,850,000,000 shares in 2001; issued and outstanding: none in 2000 and 2,967,436,680 shares in 2001	—	30
MCI group common stock, par value $.01 per share; authorized none in 2000 and 150,000,000 shares in 2001; issued and outstanding: none in 2000 and 118,595,711 in 2001	—	1
Additional paid-in capital	52,877	54,297
Retained earnings	3,160	4,400
Unrealized holding gain (loss) on marketable equity securities	345	(51)
Cumulative foreign currency translation adjustment	(817)	(562)
Treasury stock, at cost, 6,765,316 shares of WorldCom, Inc. in 2000, 6,765,316 shares of WorldCom group stock and 270,613 shares of MCI group stock in 2001	(185)	(185)
Total shareholders' investment	55,409	57,930
	$ 98,903	$ 103,914

The accompanying notes are an integral part of these statements.

WORLDCOM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In Millions, Except Per Share Data)

	For the Years Ended December 31, 1999	2000	2001
Revenues	$35,908	$39,090	$35,179
Operating expenses:			
Line costs	14,739	15,462	14,739
Selling, general and administrative	8,935	10,597	11,046
Depreciation and amortization	4,354	4,878	5,880
Other charges	(8)	—	—
Total	28,020	30,937	31,665
Operating income	7,888	8,153	3,514
Other income (expense):			
Interest expense	(966)	(970)	(1,533)
Miscellaneous	242	385	412
Income before income taxes, minority interests and cumulative effect of accounting change	1,164	7,568	2,393
Provision for income taxes	2,965	3,025	927
Income before minority interests and cumulative effect of accounting change	4,199	4,543	1,466
Minority interests	(186)	(305)	35
Income before cumulative effect of accounting change	4,013	4,238	1,501
Cumulative effect of accounting change (net of income tax of $50 in 2000)	—	(85)	—
Net income	4,013	4,153	1,501
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	72	65	117
Net income applicable to common shareholders	$ 3,941	$ 4,088	$ 1,384
Net income attributed to WorldCom group before cumulative effect of accounting change	$ 2,294	$ 2,608	$ 1,407
Cumulative effect of accounting change	$ —	$ (75)	$ —
Net income attributed to WorldCom group	$ 2,294	$ 2,533	$ 1,407
Net income (loss) attributed to MCI group before cumulative effect of accounting change	$ 1,647	$ 1,565	$ (23)
Cumulative effect of accounting change	$ —	$ (10)	$ —
Net income (loss) attributed to MCI group	$ 1,647	$ 1,555	$ (23)
Earnings (loss) per common share:		Pro Forma	
WorldCom group:			
Net income attributed to WorldCom group before cumulative effect of accounting change:			
Basic	$ 0.81	$ 0.91	$ 0.48
Diluted	$ 0.78	$ 0.90	$ 0.48
Cumulative effect of accounting change	$ —	$ (0.03)	$ —
Net income attributed to WorldCom group:			
Basic	$ 0.81	$ 0.88	$ 0.48
Diluted	$ 0.78	$ 0.87	$ 0.48
MCI group:			
Net income (loss) attributed to MCI group before cumulative effect of accounting change:			
Basic	$ 14.32	$ 13.61	$ (0.20)
Diluted	$ 14.32	$ 13.61	$ (0.20)
Cumulative effect of accounting change	$ —	$ (0.09)	$ —
Net income (loss) attributed to MCI group:			
Basic	$ 14.32	$ 13.52	$ (0.20)
Diluted	$ 14.32	$ 13.52	$ (0.20)

The accompanying notes are an integral part of these statements.

WORLDCOM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' INVESTMENT
For the Three Years Ended December 31, 2001
(In Millions)

	WorldCom, Inc. Common Stock	WorldCom Gmup Common Stock	MCI Gmup Common Stock	Additional Wid-in Capital	Retained Earnings (Deficit)	Unrealized Holding Gain (Loss)	Foreign Currency Translation Adjustment	Treasury Stock	Total Shareholders' Investment
Balances. December 31, 1998.	$ 28	$—	$—	$50,173	$(4,869)	$ 122	$ (28)	$(185)	$45,241
Exercise of stuck options (61 million shares)	—	—	—	886	—	—	—	—	886
Tax adjustment resulting from exercise of stock options.	—	—	—	820	—	—	—	—	820
Shares issued for acquisitions (4 million shares)	—	—	—	228	—	—	—	—	228
Conversion of convertible subordinated debt into common stock.	—	—	—	1	—	—	—	—	1
Other comprehensive income loss) (net of taxes and reclassificationsf:									
Net inwme	—	—	—	—	4,013	—	—	—	4,013
Distributions on mandatorily redeemable preferred Securities and other preferred dividend requirements	—	—	—	—	(72)	—	—	—	(72)
Net change in unrealized holding gain on marketable equity securities	—	—	—	—	—	453	—	—	453
Foreign currency adjustment . . .	—	—	—	—	—	—	(332)	—	(332)
Total comprehensive income									4,062
Balances, December 31, 1999	28	—	—	52,108	(928)	575	(360)	(185)	51,238
Exercise of stock options (38 million shares)	1	—	—	584	—	—	—	—	585
Tax adjustment resulting from exercise of stock options.	—	—	—	348	—	—	—	—	348
Shares issued for acquisitions (0.3 million shares)	—	—	—	27	—	—	—	—	27
Redemption of Series C preferred stock .	—	—	—	(190)	—	—	—	—	(190)
Other comprehensive income (lass) (net of taxes and reclassifications):									
Net income	—	—	—	—	4,153	—	—	—	4,153
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	—	—	—	—	(65)	—	—	—	(65)
Net change in unrealized holding gain on marketable equity securities	—	—	—	—	—	(230)	—	—	(230)
Foreign currency adjustment . . .	—	—	—	—	—	—	(457)	—	(457)
Total comprehensive income									3,401
Balances, December 31, 2000	29	—	—	52,877	3,160	345	(817)	(185)	55,409
Deconsolidation of Embratel	—	—	—	—	(2)	—	335	—	333
Recapitalization of WorldCom, Inc. common shares	(29)	29	1	(1)	—	—	—	—	—
Exercise of stock options (10 million shares)	—	—	—	124	—	—	—	—	124
Tax adjustment from exercise of stock options	—	—	—	32	—	—	—	—	32
Shares issued for acquisition—									
(67 million WorldCom group common shares)	—	1	—	1,265	—	—	—	—	1.266
(2.7 million MCI group common shares).	—	—	—	—	—	—	—	—	—
Dividends declared on MCI group common stock.	—	—	—	—	(142)	—	—	—	(142)
Other comprehensive income loss) (net of taxes and reclassificationsf:									
Net income	—	—	—	—	1,501	—	—	—	1,501
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	—	—	—	—	(117)	—	—	—	(117)
Derivative financial instruments:									
Cumulative effect of adoption of SFAS 133 as of January 1, 2001 . . .	—	—	—	—	—	28	—	—	28
Reclassification of derivative financial instruments to current earnings. . . .	—	—	—	—	—	(110)	—	—	(110)
Change in fair value of derivative financial instruments	—	—	—	—	—	82	—	—	82
Net change in unrealized holding gain (loss) on marketable equity securities .	—	—	—	—	—	(396)	—	—	(396)
Foreign currency adjustment	—	—	—	—	—	—	(80)	—	(80)
Total comprehensive income									908
Balances, December 31, 2001	$ —	$30	$ 1	$54,297	$ 4,400	$ (51)	$(562)	$(185)	$57.930

The accompanying notes are an integral part of these statements

WORLDCOM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Millions)

	For the Years Ended December 31,		
	1999	2000	2001
Cash flows from operating activities:			
Net income	$ 4,013	$ 4,153	$ 1,501
Adjustments to reconcile net income to net cash provided by operating activities:			
Cumulative effect of accounting change	—	85	—
Minority interests	186	305	(35)
Other charges	(8)	—	—
Depreciation and amortization	4,354	4,878	5,880
Provision for deferred income taxes	2,903	1,649	1,104
Change in assets and liabilities, net of effect of business combinations:			
Accounts receivable, net	(875)	(1,126)	281
Other current assets	143	(797)	164
Accounts payable and other current liabilities	692	(1,050)	(1,154)
All other operating activities	(403)	(431)	253
Net cash provided by operating activities	11,005	7,666	7,994
Cash flows from investing activities:			
Capital expenditures	(8,716)	(11,484)	(7,886)
Acquisitions and related costs	(1,078)	(14)	(206)
Increase in intangible assets	(743)	(938)	(694)
Decrcase in other liabilities	(650)	(839)	(480)
All other investing activities	1,632	(1,110)	(424)
Net cash used in investing activities	(9,555)	(14,385)	(9,690)
Cash flows from financing activities:			
Principal borrowings (repayments) on debt, net	(2,894)	6,377	3,031
Common stock issuance	886	585	124
Distributions on mandatorily redeemable and other preferred securities and dividends paid on other equity securities	(72)	(65)	(154)
Redemptions of preferred stock	—	(190)	(200)
All other financing activities	—	(84)	(272)
Net cash provided by (used in) financing activities	(2,080)	6,623	2,529
Effect of exchange rate changes on cash	(221)	(19)	38
Net increase (decrease) in cash and cash equivalents	(851)	(115)	871
Cash and cash equivalents at beginning of period	1,727	876	761
Deconsolidation of Embratel	—	—	(216)
Cash and cash equivalents at end of period	$ 876	$ 761	$ 1,416

The accompanying notes are an integral part of these statements.

WORLDCOM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31,2001

(1)The Company and Significant Accounting Policies—

Description of Business and Organization:

Organized in 1983, WorldCom, Inc., a Georgia corporation, provides a broad range of communications services to both U.S. and non-U.S. based businesses and consumers. We are a global communications company utilizing a strategy based on being able to provide service through our own facilities throughout the world instead of being restricted to a particular geographic location. We call this our "on-net" strategy. The on-net approach allows our customers to send data or voice communications across town, across the U.S., or to any of our networks in Europe or Asia, often without ever leaving our networks. The on-net approach provides our customers with superior reliability and low operating costs. Our core business is communications services, which includes voice, data, Internet and international services. We serve as a holding company for our subsidiaries' operations. References herein to WorldCom, "we,)' "our," or "us" include WorldCom, Inc. and its subsidiaries, unless the context otherwise requires.

Recapitalization:

On June 7, 2001, our shareholders approved a recapitalization involving the creation of two separately traded tracking stocks:

- WorldCom group stock, which is intended to reflect the performance of our data, Internet, international and commercial voice businesses and is quoted on The Nasdaq National Market under the trading symbol "WCOM', and
- MCI group stock, which is intended to reflect the performance of our consumer, small business, wholesale long distance voice and data, wireless messaging and dial-up Internet access businesses and is quoted on The Nasdaq National Market under the trading symbol "MCIT".

In connection with the recapitalization, we amended our articles of incorporation to replace our existing common stock with two new series of common stock that are intended to reflect, or track, the performance of the businesses attributed to the WorldCom group and the MCI group. Effective with the recapitalization on June 7, 2001, each share of our existing common stock was changed into one share of WorldCom group stock and 1/25 of a share of MCI group stock.

A tracking stock is a separate class of a company's common stock intended to provide a return to investors based upon the financial performance of a distinct business unit of the company, sometimes referred to as the targeted business. These targeted businesses are collections of businesses that we have grouped together in order for us to issue WorldCom group stock and MCI group stock. The ownership of the targeted business does not change, and while each of the classes of stock trade separately, all shareholders are common shareholders of a single company, WorldCom, and are subject to all risks of an investment in WorldCom as a whole.

During the second quarter of 2001, we declared the initial quarterly dividend for the MCI group stock. A cash dividend of $0.60 per share of MCI group stock, or approximately $70 million in the aggregate, was paid on October 15, 2001 to shareholders of record as of the close of business on September 28, 2001. Dividends of $0.60 per share of MCI group stock were also declared in the third and fourth quarters of 2001, which have been or will bc paid in 2002.

(1) The Company and Significant Accounting Policies—(Continued)

The MCI group was initially allocated notional debt of $6 billion and our remaining debt was allocated on a notional basis to the WorldCom group. We intend, for so long as the WorldCom group stock and the MCI group stock remains outstanding, to include in our filings under the Securities Exchange Act of 1934, as amended, the combined financial statements of each of the WorldCom group and the MCI group. These combined financial statements will be prepared in accordance with accounting principles generally accepted in the United States, and in the case of annual financial statements, will be audited. These combined financial statements are not legally required under current law or SEC regulations.

Voting rights of the holders of the WorldCom group and the MCI group stock are prorated based on the relative market values of WorldCom group stock and MCI group stock. We will conduct shareholder meetings that encompass all holders of voting stock. The WorldCom group and the MCI group shareholders will vote together as a single class on all matters brought to a vote of shareholders, including the election of our directors.

Our board of directors may at any time convert each outstanding share of MCI group stock into shares of WorldCom group stock at 110% of the relative trading value of MCI group stock for the 20 days prior to the announcement of the conversion. No premium will be paid on a conversion that occurs after June 7, 2004.

If all or substantially all of the WorldCom group or MCI group assets are sold, either: (i) the relevant shareholders will receive a distribution equal to the fair value of the net proceeds of the sale, either by special dividend or by redemption of shares; or (ii) each outstanding share of MCI group stock will be converted into shares of WorldCom group stock at 110% or 100% of the relative trading value of MCI group stock for a 10 trading day period following the sale.

Principles of Consolidation:

The consolidated financial statements include the accounts of WorldCom and our subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation. Investments in joint ventures and other equity investments in which we own a 20% to 50% voting ownership interest are accounted for by the equity method. Investments of less than 20% ownership, where we do not exercise control or significant influence, are accounted for under the cost method.

Embratel Deconsolidation:

During the second quarter of 2001, we reached a long-term strategic decision to restructure our investment in Embratel Participações S.A., or Embratel. The restructuring included the resignation of certain Embratel board of directors seats, the irrevocable obligation to vote a portion of our common shares in a specified manner and the transfer of certain economic rights associated with such shares to an unrelated third party. Based on these actions, the accounting principles generally accepted in the United States prohibit the continued consolidation of Embratel's results. Accordingly, we have deconsolidated Embratel's results effective January 1, 2001.

As of December 31, 2001, our carrying value for our 19.3% ownership interest in Embratel was $992 million, which is included in other assets in the accompanying consolidated financial statements.

(1) The Company and Significant Accounting Policies—(Continued)

Our equity in Embratel's loss for 2001 is included in miscellaneous income/(expense) in the accompanying consolidated financial statements.

Fair Value of Financial Instruments:

The fair value of long-term debt and company ohligatcd mandatorily redeemable and other preferred securities is determined based on quoted market rates or the cash flows from such financial instruments discounted at our estimated current interest rate to enter into similar financial instruments. The carrying amounts and fair values of these financial instruments were $25.7 billion and $25.3 billion, respectively, at Deccmher 31, 2000 and $32.2 billion and $32.9 billion, respectively, at December 31, 2001. The carrying values for all our other financial instruments approximate their respective fair values.

Cash and Cash Equivalents:

We consider cash in banks and short-term investments with original maturities of three months or less as cash and cash equivalents.

Properly and Equipment:

Property and equipment are stated at cost. Depreciation is provided for financial reporting purposes using the straight-line method over the following estimated useful lives:

Transmission equipment (including conduit)	4 to 40 years
Communications equipment	5 to 10 years
Furniture, fixtures, buildings and other	4 to 39 years

We evaluate the recoverability of property and equipment when events and circumstances indicate that such assets might be impaired. We determine impairment by comparing the undiscounted future cash flows estimated to be generated by these assets to their respective carrying amounts. In the event an impairment exists, a loss is recognized based on the amount by which the carrying value exceeds the fair value of the asset. If quoted market prices for an asset are not available, fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved. Losses on property and equipment to be disposed of are determined in a similar manner, except that fair market values are reduced for the cost to dispose.

Maintenance and repairs are expensed as incurred. Replacements and betterments are capitalized. The cost and related reserves of assets sold or retired are removed from the accounts, and any resulting gain or loss is reflected in results of operations.

We construct certain of our own transmission systems and related facilities. Internal costs directly related to the construction of such facilities, including interest and salaries of certain employees, are capitalized. Such internal costs were $625 million ($339 million in interest), $842 million ($495 million in interest) and $858 million ($498 million in interest) in 1999, 2000 and 2001, respectively.

(1) The Company and Significant Accounting Policies — (Continued)

Goodwill and Other Intangible Assets:

The major classes of intangible assets as of December 31, 2000 and 2001 are summarized below (in millions):

	Amortization Period	2000	2001
Goodwill	5 to 40 years	$44,870	$49,825
Tradenames	40 years	1,100	1,112
Developed technology.	5 to 10 years	2,100	2,100
Other intangibles	5 to 10 years	3,778	4,857
		51,848	57,894
Less: accumulated amortization		(5,254)	(7,357)
Goodwill and other intangible assets, net		$46,594	$50,537

Intangible assets are amortized using the straight-line method for the periods noted above.

Goodwill is recognized for the excess of the purchase price of the various business combinations over the value of the identifiable net tangible and intangible assets acquired. Realization of acquisition-related intangibles, including goodwill, is periodically assessed by our management based on the current and expected future profitability and cash flows of acquired companies and their contribution to the overall operations of WorldCom.

Also included in other intangibles are costs incurred to develop software for internal use. Such costs were $710 million, $925 million and $689 million for the years ended December 31, 1999, 2000 and 2001, respectively.

Investments in Marketable Equity Securities:

Investments in marketable equity securities are classified as available-for-sale securities and reported at fair value. Unrealized holding gains and losses, net of taxes, are reflected as a component of shareholders' investment in the accompanying consolidated financial statements.

Foreign Currency Translation:

Assets and liabilities recorded in foreign currencies are translated at the exchange rate as of the balance sheet date. Translation adjustments are recorded as a separate component of shareholders' investment. All revenue and expense accounts are translated at a weighted-average of exchange rates in effect during the period. Transaction gains and losses that arise from exchange rate fluctuations on transactions denominated in a currency other than the functional currency are included in the results of operations as incurred. The accompanying consolidated statements of operations include foreign currency transaction losses, after elimination of minority interests, of $36 million and $38 million for the years ended December 31, 1999 and 2000, respectively, and foreign currency transaction gains of $9 million for the year ended December 31, 2001.

(1) The Company and Significant Accounting Policies — (Continued)

Recognition of Revenues:

We record revenues for telecommunications services at the time of customer usage. Service activation and installation fees are amortized over the average customer contract life.

Accounting for International Long Distance Traffic and Other:

We enter into operating agreements with telecommunications carriers in foreign countries under which international long distance traffic is both delivered and received. The terms of most switched voice operating agreements, as well as established FCC policy, require that inbound switched voice traffic from the foreign carrier to the United States be routed to United States international carriers, like WorldCom, in proportion to the percentage of United States outbound traffic routed by that United States international carrier to the foreign carrier. Mutually exchanged traffic between us and foreign carriers is settled in cash through a formal settlement policy that generally extends over a six-month period at an agreed upon settlement rate. International settlements are treated as an offset to line costs. This reflects the way in which the business is operated because WorldCom actually settles in cash through a formal net settlement process that is inherent in the operating agreements with foreign carriers.

Reciprocal compensation represents a reimbursement of costs for call termination performed on behalf of other carriers' customers and is determined contractually based on fixed rate per minute charges to those carriers. Small business and consumer primary interexchange carrier charges, or PICC, are flat-rate charges mandated by the FCC which apply to telecommunications companies that connect to customers through a traditional phone company's facilities. Effective July 1, 2000, as a result of the FCC's Coalition for Affordable Local and Long Distance Services, or CALLs order, the PICC fee is billed directly to the customer by the traditional phone company rather than to WorldCom and rebilled to the customer. Central office based remote access equipment sales represent the reimbursement of customet specific equipment costs incurred by WorldCom on behalf of the customer as part of service provisioning. As such, WorldCom determined that it is more appropriate to reflect all of these reimbursements of our cost as an offset to line costs rather than reporting these reimbursements on a gross basis as revenues. During the years ended December 31, 1999, 2000 and 2001, such amounts totaled $1.2 billion, $1.2 billion and $614 million, respectively.

Derivative Financial Instruments:

Effective January 1, 2001, we adopted the Financial Accounting Standards Board's, or FASB's, Statement of Financial Accounting Standard, or SFAS, No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. This statement establishes accounting and reporting standards requiring that derivative instruments (including certain derivative instruments embedded in other contracts) he recorded in the balance sheet as either an asset or liability measured at fair value. As of January 1, 2001, our exposure to derivative financial instruments primarily consisted of option collar transactions designated as cash flow hedges of anticipated sales of an equity investment, which we maintain to minimize the impact of adverse changes in the market price of the related equity investment, The initial adoption of SFAS No. 133 provided a net transition gain from our designated cash flow hedges resulting in an increase in other comprehensive income of approximately $28 million. During 2001, shares of the hedged equity investment were sold and we reclassified respective hedging

(1) The Company and Significant Accounting Policies—(Continued)

gains of $110 million from accumulated comprehensive income to miscellaneous income. As of December 31, 2001, we maintain no derivative financial instruments. No amounts were reclassified to earnings resulting from any ineffective portion of the designated derivative hedges or from the discontinuance of designation of any cash flow hedges.

Cumulative Effect of Accounting Change:

During the fourth quarter of 2000, we implemented Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements", or SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather than be recognized immediately. Costs directly related to these revenues may also be deferred and amortized over the customer contract lie. As required by SAB 101, we retroactively adopted this accounting effective January 1, 2000, which resulted in a one-time expense of $85 million, net of income tax benefit of $50 million. The pro forma effect of adopting SAB 101 on periods prior to January 1, 2000 was not material to our consolidated financial position or results of operations.

Income Taxes:

We recognize current and deferred income tax assets and liabilities based upon all events that have been recognized in the consolidated financial statements as measured by the provisions of the enacted tax laws.

Earnings Per Share:

Our consolidated financial statements present basic and diluted earnings (loss) per share for WorldCom group stock and MCI group stock using the two-class method. The two-class method is an earnings formula that determines the attributed earnings (loss) per share for WorldCom group stock and MCI group stock according to participation rights in undistributed earnings. The combined financial statements of the WorldCom group and the MCI group do not separately present earnings (loss) per share because WorldCom group stock and MCI group stock are series of our common stock, and the WorldCom group and the MCI group are not legal entities with a capital structure.

For purposes of our consolidated financial statements, basic earnings (loss) per share attributed to WorldCom group stock and MCI group stock is computed by dividing the respective attributed net income (loss) for the period by the respective number of weighted-average shares of WorldCom group stock and MCI group stock then outstanding. Diluted earnings (loss) per share attributed to WorldCom group stock and MCI group stock is computed by dividing the respective attributed net income (loss) for the period by the respective weighted-average number of shares of WorldCom group stock and MCI group stock outstanding, including the respective dilutive effect of WorldCom group stock and MCI group stock equivalents.

(1) The Company and Significant Accounting Policies — (Continued)

The following is a reconciliation of the numerators and the denominators of the basic and diluted earnings (loss) per share computations for the WorldCom group and the MCI group for the years ended December 31, 1999, 2000 and 2001 (in millions, except per share data):

	Pro Forma		
	1999	**2000**	**2001**
WORLDCOM GROUP STOCK			
Basic			
Income attributed to WorldCom group before cumulative effect of accounting change	$2,366	$2,673	$1,524
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	72	65	117
Net income attributed to WorldCom group before cumulative effect of accounting change	$2,294	$2,608	$1,407
Weighted-average shares of WorldCom group stock outstanding	2,821	2,868	2,923
Basic earnings per share attributed to WorldCom group stock before cumulative effect of accounting change	$ 0.81	$ 0.91	$ 0.48
Diluted			
Net income attributed to WorldCom group before cumulative effect of accounting change	$2,294	$2,608	$1,407
Weighted-average shares of WorldCom group stock outstanding	2,821	2,868	2,923
WorldCom group stock equivalents	102	42	9
WorldCom group stock issuable upon conversion of preferred stock	2	2	1
Diluted shares of WorldCom group stock outstanding	2,925	2,912	2,933
Diluted earnings per share attributed to WorldCom group stock before cumulative effect of accounting change	$ 0.78	$ 0.90	$ 0.48
MCI GROUP STOCK			
Basic and Diluted			
Net income (loss) attributed to MCI group before cumulative effect of accounting change	~~$1,647~~	~~$1,565~~	~~$ (23)~~
Basic and diluted weighted-average MCI group shares outstanding	115	115	117
Basic and diluted earnings (loss) per share attributed to MCI group stock before cumulative effect of accounting change	$14.32	$13.61	$(0.20)

As discussed above, the recapitalization of WorldCom was effective June 7, 2001, and each share of WorldCom stock was changed into one share of WorldCom group stock and 1/25 of a share of MCI group stock. The weighted-average shares outstanding and attributed earnings (loss) per share information above is pro forma and assumes the recapitalization occurred **at** the beginning of 1999 and the WorldCom group stock and MCI group stock existed for all periods presented.

(1) The Company and Significant Accounting Policies — (Continued)

Stock Splits:

On November 18, 1999, our board of directors authorized a three-for-hvo stock split in the form of a 50% stock dividend which was distributed on December 30, 1999 to shareholders of record on December 15, 1999. All per share data and numbers of common shares have been retroactively restated to reflect this stock split.

Concentration of Credit **Risk:**

A portion of our revenues is derived from services provided to others in the telecommunications industry, mainly resellers of long distance telecommunications service and Internet online services. As a result, we have some concentration of credit risk among our customer base. We perform ongoing credit evaluations of our larger customer's financial condition and, at times, require collateral from our customers to support our receivables, usually in the form of assignment of our customers' receivables to us in the event of nonpayment.

Recently Issued Accounting Standards:

In June 2001, the FASB issued SFAS No. 141 "Business Combinations" and SFAS No. 142 "Goodwill and Other Intangible Assets." SFAS No. 141 requires business combinations initiated after June 30, 2001, which includes the Intermedia merger. to be accounted for using the purchase method of accounting and broadens the criteria for recording intangible assets separate from goodwill. Recorded goodwill and intangibles will bc evaluated against this new criteria and may result in certain intangibles being subsumed into goodwill, or alternatively, amounts initially recorded as goodwill may be separately identified and recognized apart from goodwill. Under the new rules, goodwill and intangible assets deemed to have indefinite lives will no longer be amortized but will be subject to annual impairment tests. The statement includes provisions for the identification of reporting units for purposes of assessing potential future impairments of goodwill. Upon adoption, we stopped amortizing intangible assets with indefinite useful lives, including goodwill and tradenames. Based on current levels of such assets, this will reduce amortization expense by approximately $1.3 billion annually ($1.0 billion at the WorldCom group and $0.3 billion at the MCI group). Additionally, we are conducting impairment reviews of all intangible assets with indefinite useful lives and we expect to complete this assessment no later than the second quarter of 2002, in accordance with the provisions of SFAS No. 142. Based on our preliminary analyses, we estimate that as a result of the adoption of SFAS No. 142 we will reduce goodwill by $15 to $20 billion, with approximately $1 billion of the reduction at the MCI group.

In June 2001, the FASB issued SFAS No. 143 "Asset Retirement Obligations," which establishes new accounting and reporting standards for legal obligations associated with retiring assets. The fair value of a liability for an asset retirement obligation must be recorded in the period in which it is incurred, with the cost capitalized as part of the related long-lived assets and depreciated over the asset's useful life. Changes in the liability resulting from the passage of time will be recognized as operating expenses. SFAS No. 143 must be adopted by 2003. We have not yet quantified the impact of adopting SFAS No. 143 on our consolidated results of operations or financial position.

(1) The Company and Significant Accounting Policies — (Continued)

In August 2001, the FASB issued SFAS No. 144 "Accounting for the Impairment or Disposal of Long Lived Assets," which supersedes both SFAS No. 121 'Accounting for the Impairment of Long-Lived Assets for Long-Lived Assets to be Disposed Of," and the accounting and reporting provisions for the disposal of a segment of a business contained in APB Opinion No. 30, "Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions." SFAS No. 144 establishes a single accounting model for long-lived assets to be disposed of by sale and broadens the presentation of discontinued operations. The provisions of SFAS No. 144 are effective beginning in 2002 and are not expected to have a material impact on our consolidated results of operations or financial position.

Use of Estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States, or GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the period reported. Actual results could differ from those estimates. Estimates are used when accounting for allowance for doubtful accounts, revenue reserves, depreciation and amortization, taxes and contingencies.

(2) Business Combinations—

We have acquired other telecommunications companies offering similar or complementaly services to those offered by us. These acquisitions have been accomplished through the purchase of the outstanding stock or assets of the acquired entity for cash, notes, shares of our common stock, or a combination thereof. The cash portion of acquisition costs has generally been financed through our bank credit facilities.

On July 1, 2001, we acquired Intermedia Communications Inc. for approximately $5.8 billion, including assumed long-term debt, pursuant to the merger of a wholly owned subsidialy with and into Intermedia, with Intermedia continuing as the surviving corporation and as a subsidiary of WorldCom. As a result of the Intermedia merger, we acquired a controlling interest in Digex, Incorporated, or Digex, a provider of managed Web and application hosting services. In connection with the Intermedia merger, stockholders of Intermedia received one share of WorldCom group stock (or 57.1 million WorldCom group shares in the aggregate) and 1/25th of a share of MCI group stock (or 2.3 million MCI group shares in the aggregate) for each share of Intermedia common stock they owned. Holders of Intermedia preferred stock, other than Intermedia's 13.5% Series B Redeemable Exchangeable Preferred Stock due 2009, or Intermedia Series B Preferred Stock, received one share of a class or series of our preferred stock, with substantially identical terms, which were established upon consummation of the Intermedia merger. As a result of the merger with Intermedia, we own approximately 90% of the voting securities of Intermedia.

Upon effectiveness of the merger with Intermedia, the then outstanding and unexercised options for shares of Intermedia common stock were converted into options exercisable for an aggregate of approximately 10 million shares of WorldCom group stock having the same terms and conditions as the Intermedia options, except that the exercise price and the number of shares issuable upon exercise

(2) Business Combinations — (Continued)

were divided and multiplied, respectively, by 1.0319. The merger with Intermedia was accounted for as a purchase and was allocated to the WorldCom group.

The purchase price in the Intermedia merger was allocated based on appraised fair values at the date of acquisition. This resulted in an excess purchase price over net assets acquired of $5.1 billion of which $67 million was allocated to customer lists, which will be amortized over approximately four years on a straight line basis. The remaining excess of $5.0 billion has been allocated to goodwill and tradename which are not subject to amortization and the goodwill is not expected to be deductible for tax purposes.

In connection with the Intermedia merger, the Antitrust Division of the Department of Justice required us to dispose of Intermedia's Internet service provider business, which provided integrated Internet connectivity solutions, and effective December 1, 2001, we sold substantially all of the Internet related assets for approximately $12 million. In addition to this required divestiture, we also committed to a plan to sell Intermedia's Advanced Building Network business, which provides centralized telecommunications services in multi-tenant commercial office buildings, and the systems integration business through which Intermedia sells, installs, operates and maintains business telephony customer premise equipment for its customers. We included the appraised fair values of these assets to be disposed of in our initial allocation of the Intermedia purchase price and also included accrued anticipated losses expected to be incurred through disposal date. Any difference between the actual results of operations and the amounts accrued will result in an adjustment of goodwill unless there is a difference resulting from a post-merger event. For the year ended Deccmbcr 31, 2001, operating losses for these assets to be disposed of were approximately $41 million, before corporate allocations. We anticipate that we will complete the planned disposals of the remaining identified businesses before the third quarter of 2002.

On October 1, 1999, we acquired SkyTel Communications, Inc., pursuant to the merger of SkyTel with and into a wholly owned subsidiary of WorldCom. Upon consummation of the SkyTel merger, the wholly owned subsidiary was renamed SkyTel Communications, Inc. SkyTel is a leading provider of nationwide messaging services in the United States. SkyTel's principal operations include one-way messaging services in the United States, advanced messaging services on the narrow band personal communications services network in the United States and international one-way messaging operations.

As a result of the SkyTel merger, each outstanding share of SkyTel common stock was converted into the right to receive 0.3849 shares of WorldCom common stock, par value $.01 per share, or approximately 23 million WorldCom common shares in the aggregate. Holders of SkyTel's $2.25 Cumulative Convertible Exchangeable Preferred Stock, received one share of WorldCom Series C $2.25 Cumulative Convertible Exchangeable Preferred Stock for each share of SkyTel preferred stock held. The SkyTel merger was accounted for as a pooling-of-interests; and accordingly, our financial statements for periods prior to the SkyTel merger have been restated to include the results of SkyTel. SkyTel has been allocated to the MCI group.

(2) Business Combinations — (Continued)

During 1999, 2000 and 2001, we recorded other liabilities of $582 million, $29 million and $254 million, respectively, related to estimated costs of unfavorable commitments of acquired entities, and other non-recurring costs arising from various acquisitions and mergers. At December 31, 1999, 2000 and 2001, other liabilities related to these and previously recorded accruals totaled $1.8 billion, $938 million and $817 million, respectively.

(3) Investments—

As of December 31, 2000 and 2001, our investments in marketable equity securities are included in other assets at their fair value of approximately $970 million and $22 million, respectively. The unrealized holding gain or **loss** on these marketable equity securities, net of taxes of $207 million and tax benefits of $31 million **as** of December 31, 2000 and 2001, respectively, is included as a component of shareholders' investment in the accompanying consolidated financial statements. **As** of December 31, 2000 and 2001, the gross unrealized holding gain on these securities was $716 million and $2 million, respectively. The gross unrealized holding **loss** on these securities was $164 million and $83 million at December 31, 2000 and 2001, respectively. Proceeds from the sale of marketable equity securities totaled $1.7 billion, $680 million and $526 million for the years ended December 31, 1999, 2000 and 2001, respectively. Gross realized gains on marketable equity securities, which represent reclassification adjustments to other comprehensive income, were $374 million, $643 million and $380 million for the years ended December 31, 1999, 2000 and 2001, respectively. Gross realized losses were $25 million and $2 million for the years ended December 31, 2000 and 2001, respectively. There were no gross realized losses for the ycar ended December 31, 1999.

Other cost investments totaled $1.2 billion and $1.0 billion as of December 31, 2000 and 2001, respectively. Dividend income recorded on cost investments for the years ended December 31, 1999, 2000 and 2001 was $32 million, $22 million and ***$56*** million, respectively.

In the second quarter of 2001, we recorded a pre-tax charge of $865 million related to the write-off of investments in specific publicly traded and privately held companies. The write-off represented an other than temporary impairment in the carrying value of the identified investments resulting from bankruptcies and other declines in the telecommunications industry.